44026

MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2018/2019

BAC4644 – ADVANCED TAXATION

(All sections / Groups)

4 MARCH 2019
9.00 a.m – 12.00 p.m.
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 8 (EIGHT) pages (excluding the cover page) with 4 (FOUR) Questions only.

2. Attempt **ALL** questions. The distribution of the marks for each question is given.

3. Please write all your answers in the Answer Booklet.

QUESTION 1

a) Nathan was a businessman carrying on two businesses: one selling stationery and another business selling leather handbag. He passed away in a plane accident in 2016, leaving behind his wife and four children. He had also left a will creating a trust, and his wife was named as the trustee and their four children as the beneficiaries.

Under the terms of the will, one quarter of the trust income is to be distributed to the first child at the discretion of the trustee. The balance must be distributed equally between the second and third child. A sum of RM 36,000 is to be accumulated each year for the fourth child, now aged three years until the child reaches the age of 18 years. The will provided the wife with an annuity of RM 24,000 per year.

Nathan had some investments from which are derived interest, dividend and rent. The details of the business and the investment income for the year ended 31 December 2018 are as follows:

Business 1: Stationery : 1 January 2018 - 31 December 2018

	RM
Gross income	765,625
Allowable expenses	328,125
Capital allowances due for the YA 2018	65,625
Balancing charges	21,875
Balancing allowances	32,813

Business 2: Leather handbags: 1 January 2018 to 31 December 2018

	RM
Gross income	109,375
Allowable expenses	126,875
Capital allowances due for the YA 2018	13,125
Adjusted loss b/f	21,875
Capital allowances b/f	10,938

Other income

	RM
Rent	22,000
Interest	6,563
Dividends (Malaysia) (single tier)	8,000
Dividends (Singapore) not remitted	4,000

During the year, the trust paid a cash donation of RM 1,000 to an approved institution and RM 2,000 to a poor relative of Nathan during Chinese New Year.

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Based on the trust distributable income of RM 300,000 before accumulation, the trustee made the following payments to the beneficiaries for the year ended 31 December 2018: a sum of RM 70,000 to the first child and RM 110,000 each to the second and third child.

The trustee also incurred management fee of RM 3,000 during the year for executing the trust.

Required

Compute the chargeable income of the trust for the year of assessment 2018 assuming that section 61(2) of the Income Tax Act 1967 (as amended) is applied.

(16 marks)

b) Mr. Muthu owns several properties from which he received rentals. He decided to settle his properties and the income therefrom among his children in the following manner:

1st Son – Mr. Gopal

Mr. Gopal is married and is 42 years old. Under the terms of the settlement, Mr. Gopal is to receive the income from the properties so long as he lives. On his death, the properties and the right to income would revert to Mr. Muthu.

2nd Son – Mr. Subra

Mr. Subra is 22 years old and is married. Under the terms of the settlement, Mr. Muthu can revoke the settlement anytime

Daughter – Ms Rajees

Ms Rajees is 20 years old and unmarried. Under the terms of settlement she has absolute right to her share of properties and the income

Required:

Explain who would be assessed on the income in respect of the above settlements.

(4 marks)

(Total: 20 marks)

Continued...

QUESTION 2

On 4 June 2017, you and your tax principal participated in a conference call with the senior management of Pluto Sdn Bhd (Pluto), an investment holding company. Below are extracts from the notes of the conference call and an email from your tax principal to you, his tax assistant.

Extract of conference call:

Pluto Sdn Bhd (Pluto), an investment holding company, has identified Mars Sdn Bhd (Mars), a Malaysian resident, as a suitable investment. Currently, Pluto and Mars are unrelated.

Mars has been manufacturing solar panels for two years and has an accumulated tax loss of RM6.4 million and unabsorbed capital allowances (CA) of RM1 million as at the year ended 31 May 2017.

Apart from the solar panel manufacturing business, Mars does not have any other assets or sources of income.

Mars expects to make an accounting profit of about RM8.9 million in the year ended 31 May 2018. The negotiated price for Pluto either to purchase Mars's shares or take over Mars's manufacturing business (purchase of assets and liabilities) is RM75 million.

Whichever alternative is chosen, Pluto will finance the acquisition with a loan of RM55 million from its non-resident parent company and RM20 million from a Malaysian commercial bank. The annual interest rates on these loans will be 11.5% and 7% respectively.

Pluto would like to know what difference there would be from an income tax perspective if it acquires the entire share capital of Mars (**Option 1**) as compared to acquiring all the business assets and liabilities of Mars's manufacturing business (**Option 2**).

Email from tax principal:

Please draft a letter to the managing director of Pluto regarding the proposed investment in Mars.

Consider the two options for the proposed acquisition:

Option 1: Pluto will acquire 100% of the share capital of Mars for RM75 million; or

Option 2: Pluto will acquire all the assets and liabilities of the manufacturing business of Mars for RM75 million.

The issues you should consider for each option are:

(i) the form of income derived from the investment in Mars by Pluto;

(ii) the deductibility of the interest expense for Pluto;

(iii) any transfer pricing issue/s;

(iv) the treatment of the trade receivables and inventory

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(v) Mars's unabsorbed loss and CA brought forward; and

(vi) comparative tax computations

To demonstrate the differences in the income tax treatment under the two options, I suggest that you support your explanations to the client with comparative tax computations of the chargeable income of Mars business after taking into account the interest expense for the Mars manufacturing business for the year of assessment (YA) 2018.

For this purpose, you should assume that the tax adjusted income for the business under both options for YA 2018 will be RM8.8 million before taking into account the interest expense;

and the current year CA is RM200,000 if the business remains within Mars (Option 1), and RM440,000 if the business is owned by Pluto (Option 2).

(vii) Tax planning advice/ideas

Lastly, assuming that Option 2 is adopted, identify any possible tax planning advice/ideas with regard to the interest rate on the loan from Pluto's non-resident parent company and the trade receivables and the inventory to be taken over.

Required:

You, as a tax assistant, are to draft a letter to the managing director of Pluto Sdn Bhd as requested by the tax principal by considering the following issues:

(i) Form of income derived by Pluto from the investment. **(2 marks)**

(ii) Deductibility of the interest expense. **(4 marks)**

(iii) Transfer pricing issues. **(4 marks)**

(iv) Trade receivables and inventory. **(6 marks)**

(v) Unabsorbed loss and capital allowances brought forward. **(6 marks)**

(vi) Comparative computations of chargeable income. **(4 marks)**

(vii) Tax planning advice/ideas. **(4 marks)**

(Total 30 marks)

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QUESTION 3

a) Nahoda Shipping Sdn Bhd. (NSSB) is a resident Malaysian shipping company and operates two Malaysian registered ships which are N1 and N2. The following is the financial information of the company for the year ended 31 December 2018:

	Ship N1		**Ship N2**	
	RM		**RM**	
Freight income	850,000		560,000	
Voyage charter hire charges	410,000		-	
		1,260,000		560,000
Less: Expenses				
Repair and maintenance	106,000		99,000	
Depreciation	95,000		54,000	
Remuneration	180,000		87,000	
Rental	88,000		-	
Shipping agent charges	97,000		32,000	
Harbor charges	104,000		79,000	
Miscellanious expenses	120,000	(790,000)	83,000	(434,000)
Net profit		**470,000**		**126,000**

Additional information:

Miscellaneous expenses are revenue in nature and therefore deductible. Current year capital allowances for N1 and N2 are RM105,000 and RM68,000 respectively. N2 has capital allowance brought forward from year of assessment 2017 amounting to RM12,000. During the year, the company also received interest income from its investment of RM200,000 and rental income of RM160,000. The company made cash donation to an approved institution of RM65,000. It qualifies for the tax exemption.

Required:

(i) Compute the chargeable income and exempt income of NSSB for the year of assessment 2018.

(8 marks)

(ii) Explain the conditions to claim for tax exemption on 70% of statutory income under Section 54A Income Tax Act 1967 (as amended).

(4 marks)

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b) FlyAway Airline Limited (FAL) is a non-Malaysian tax resident and managed to produce a certificate from its home country's tax authority. The certificate showed the total world gross income of RM35 million, Malaysia gross income of RM1 million, world taxable income of RM18 million and world capital allowance of RM2.2 million.

Required:

Compute the income tax payable of FAL using:
(i) acceptable ratio method; and
(ii) 5 % method

(8 marks)

(Total: 20 marks)

QUESTION 4

a) Diamond Holdings Berhad (DHB) is tax resident company in Malaysia and carries on activities mainly in the holding of investments. The income statement of the company for the year ended 31 December 2018 shows the following:

	Note	RM	RM
Gross income			
Interest income	1	309,000	
Rent	2	450,000	
Dividend	3	189,000	
Gains from the sale of investment		123,000	
			1,071,000
Less: **Expenses**			
Directors fees		95,000	
Entertainment for directors		56,000	
Salaries, wages and allowances		188,000	
Management fees		54,000	
Maintenance expenses of properties	2	145,800	
Audit and accounting fees		56,000	
Depreciation		102,000	(696,800)
Profit before taxation			374,200

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Notes:

1) The company received this interest income from its debenture loan. No exemption given to this interest income.
2) The rental income is in respect of letting out properties and no full support or maintenance services are provided. The maintenance expenses of RM145,800 is incurred wholly for the rented properties.
3) Dividend income consist of single-tier dividend from Malaysia and dividend received from Singapore amounting to RM100,000 and RM89,000 respectively.

Required:

(i) Based on the information given, determine whether DHB is an investment holding company for the year of assessment 2018. State your reasons. **(4 marks)**

(ii) Based on your answer in (i), compute the income tax payable of DBH for the year of assessment 2018.

(10 marks)

(iii) Discuss THREE (3) differences between unlisted and listed investment holding companies.

(6 marks)

b) The following is the Income Statement of HartaTanah Sdn. Bhd. (HTSB), an approved real estate investment trust for the year ended 30 June 2018.

	RM	RM
Rental income		1,050,000
Interest income received from a bank		360,000
Interest income from a convertible loan stock		780,000
Dividends (Malaysian single tier)		36,000
Revaluation surplus		95,000
Gains from the realisation of securities		88,000
Total gross income		2,409,000
Less: Expenditure		
Audit and accounting fee	95,000	
Insurance premium on buildings let out	58,600	
Depreciation	96,300	
Management remuneration	120,000	
Telephone, printing and stationery	36,000	
Salaries and allowances	480,500	
Trustee administration fee	66,000	

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Approved donation	35,000	
Provision on unrealised loss on revaluation of securities	74,000	(1,061,400)
Profit before taxation		1,347,600

Capital allowance for the year is RM95,800. On 2 July 2018, HTSB distributed 65% of the total income to unit holders who are non-resident companies and resident companies.

Required:

(i) Compute the chargeable income of HTSB for the year of assessment 2018.

(8 marks)

(ii) State the tax treatment applicable to the unit holders on the distribution made on 2 July 2018.

(2 marks)

(Total 30 marks)

APPENDIX

SUPPLEMENTARY INSTRUCTIONS

1. Company tax rate at 24%
2. Calculations and workings should be made to the nearest RM.
3. All workings should be shown.

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